

STATE OF IOWA
DEPARTMENT OF COMMERCE
UTILITIES BOARD

IN RE: IES UTILITIES INC.	DOCKET NO. WRU-98-39-151
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ORDER AFFIRMING WAIVER EXTENSION

(Issued July 27, 2001)

On March 21, 2001, the Utilities Board (Board) granted IES Utilities Inc. (IES) a two-year extension of a waiver of two of the electric flexible rate rules, 199 IAC 20.14(3)"b" and "c," with respect to a contract with one of IES' customers, Keokuk Ferro-Sil (Ferro-Sil). The flexible rate rules provide that the ceiling for all discounted rates shall be the approved rate on file for the customer's rate class and that the floor for the discount rate shall be equal to the energy costs and customer costs of serving a specific customer. The Ferro-Sil contract is unique because it bases the price of electricity on a portion of Ferro-Sil's operating costs, not IES' cost of service to produce electricity. The price paid by Ferro-Sil for electricity will vary depending on its operating cost and could be above or below the price ceiling and price floor.

The Consumer Advocate Division of the Department of Justice (Consumer Advocate) filed an application for rehearing on April 6, 2001. Consumer Advocate requested rehearing on two issues: 1) The Board's deferral of determination of a contract price floor to a rate case proceeding, and 2) does the Ferro-Sil contract

violate Iowa Code § 476.5, which provides, in part, that "[n]o . . . public utility shall make or grant any unreasonable preferences or disadvantages as to the rates or services to any person or subject any person to any unreasonable preference or disadvantage." IES filed an answer to the application for rehearing on April 20, 2001

The Board on May 3, 2001, granted rehearing to take additional evidence. The Board in its order said that the economics of the Ferro-Sil contract might have changed such that rehearing is warranted. The Board's order directed IES to file additional information, which was filed on May 15, 2001, and set a hearing date.

On June 5, 2001, the day before the hearing was scheduled, IES filed a contract amendment. The hearing was delayed until July 6, 2001, to allow Consumer Advocate time for additional discovery.

The contract amendment changed the definition of production costs, which is IES' interpretation of the floor price under the Board's flexible rate rules. Consumer Advocate and IES have disagreed throughout this proceeding on what is included in the floor price calculation. The Board in its March 21, 2001, order did not determine the floor price, saying that this was an issue for determination in a rate case in the event IES sought recovery of any of the Ferro-Sil discounts. However, at rehearing, it appeared that the parties now agree on what should be included in the floor price, at least after January 1, 2002.

For the remainder of 2001, the contract amendment defines production costs to include not only variable costs for fossil fuel plants but also IES' nuclear plant, Duane Arnold Energy Center. Beginning on January 1, 2002, production costs are

defined to further include purchase power costs, both energy and demand. The definition after January 1, 2002, is the definition sought by Consumer Advocate. (Tr. 37, 42-44). The contract amendment increases the amount paid by Ferro-Sil immediately, with an additional, substantial increase on January 1, 2002.

The second issue raised by Consumer Advocate on rehearing is whether the Ferro-Sil contract is unreasonably discriminatory. While this contract is unique, IES is required under the flexible rate rules to offer this contract to any direct competitor of Ferro-Sil. The Ferro-Sil contract is consistent with the flexible rate rules to the extent that IES has assumed the risk and has agreed not to seek recovery for the discount beyond that which is allowed under the flexible rate rules. The contract is not unreasonably discriminatory when viewed in the context of the Board's flexible rate rules, particularly with the price increase effective January 1, 2002.

The Board's concern in granting rehearing was that the economics of the contract had changed since the March 21, 2001, order. One of the unique features of this contract is that it allows IES, if prices for the commodity ferrosilicon reached certain levels, to charge more than its tariffed rate and presumably "make-up" any discounts previously granted when the commodity price was low. However, testimony from Ferro-Sil's president indicated that due to the current state of the industry, the price ceiling would never be reached and Ferro-Sil would not pay more than the tariffed rate. (Tr. 15, 29).

While commodity prices for ferrosilicon are not likely to increase in the near future, Ferro-Sil is diversifying into new product lines. Sales for the new lines have

not reached projections but are steadily increasing. (Tr. 8-9, 16-17). Ferro-Sil was out of operation for a portion of this spring due to the Mississippi River flooding, which hurt the new product offering. (Tr. 10). Ferro-Sil anticipates that it will be profitable if its new product lines grow as expected. (Tr. 19).

The Board is pleased that the parties have resolved their differences on the price floor calculation, at least after January 1, 2002. Resolution of this issue between IES and Consumer Advocate provides some certainty as to the amount of the discount for which IES could potentially seek recovery in a rate proceeding. IES previously agreed to absorb any discounts below the price floor. However, IES has not agreed to absorb discounts between the price floor and its tariffed rate.

While the Board continues to view any recovery of discounts as a rate issue, the rate case recovery issue in general, in addition to the price floor discussed above, was tangentially addressed in these proceedings. Based on the testimony from IES' witness in this proceeding, the Board is somewhat skeptical that a case can be made that ratepayers benefit from the Ferro-Sil discounts. (Tr. 44-48). However, this is an issue that will be fully litigated in a rate case proceeding in the event IES seeks recovery of the difference between the price floor and tariffed rate.

Based on the testimony at the rehearing, the Board will affirm its decision to extend the waiver for a two-year period to December 31, 2002. The contract amendment alleviates the Board's concerns about the size of the discounts after January 1, 2002. As noted by Consumer Advocate's witness, no direct subsidy to Ferro-Sil from other ratepayers is likely unless recovery of the discounts is allowed in

a rate case. (Tr. 63). While the record shows some questions about the future viability of Ferro-Sil, the Board believes it is moving in the right direction in developing new product lines that are not tied to the commodity price for ferrosilicon.

The Board notes that at the expiration of this waiver period Ferro-Sil will have been receiving significant discounts since January 1, 1999. While the Board recognizes that another request may be filed to extend the waiver, the Board would expect the discount to decrease, or at least not to increase. Four years should be a sufficient amount of time for Ferro-Sil to make changes to its business such that it can operate profitably without a significant electric rate discount.

IT IS THEREFORE ORDERED:

The Board's order in this docket, issued March 21, 2001, granting IES Utilities Inc. a two-year extension of a waiver of 199 IAC 20.14(3)"b" and "c" to December 31, 2002, is affirmed on rehearing.

UTILITIES BOARD

/s/ Allan T. Thoms

/s/ Diane Munns

ATTEST:

/s/ Judi K. Cooper
Acting Executive Secretary

Dated at Des Moines, Iowa, this 27th day of July, 2001